

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-71425; File No. SR-NYSEArca-2014-04)

January 28, 2014

Self-Regulatory Organizations; NYSE Arca, Inc.; Notice of Filing of Proposed Rule Change to Amend its Rules by Revising the Order of Priority of Bids and Offers when Executing Orders in Open Outcry

Pursuant to Section 19(b)(1)<sup>1</sup> of the Securities Exchange Act of 1934 (the “Act”)<sup>2</sup> and Rule 19b-4 thereunder,<sup>3</sup> notice is hereby given that, on January 15, 2014, NYSE Arca, Inc. (the “Exchange” or “NYSE Arca”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of the Substance of the Proposed Rule Change

The Exchange proposes to amend its rules by revising the order of priority of bids and offers when executing orders in open outcry. The text of the proposed rule change is available on the Exchange’s website at [www.nyse.com](http://www.nyse.com), at the principal office of the Exchange, and at the Commission’s Public Reference Room.

II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of those statements may be examined at the places

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<sup>1</sup> 15 U.S.C.78s(b)(1).

<sup>2</sup> 15 U.S.C. 78a.

<sup>3</sup> 17 CFR 240.19b-4.

specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant parts of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The Exchange proposes to amend its rules governing the priority of bids and offers on the Consolidated Book by revising the order of priority of bids and offers for orders in open outcry. Specifically, the Exchange proposes to afford priority to bids and offers represented by Market Makers and Floor Brokers ("Crowd Participants") over certain equal-priced bids and offers of non-Customers<sup>4</sup> on the Consolidated Book<sup>5</sup> during the execution of an order in open outcry on the floor of the Exchange.

Current Rule 6.75(a) provides that any bids displayed on the Consolidated Book have priority over same-priced bids represented in open outcry. Such priority is also described in Rule 6.47, which governs crossing orders in open outcry. Floor Broker crossing transactions, as defined in Rule 6.47, may not trade ahead of equal and better-priced bids or offers on the Consolidated Book.

Because of the priority afforded to the Consolidated Book, Crowd Participants who have negotiated a large transaction ultimately may not participate in the execution. Crowd Participants could negotiate a transaction with an understanding of the make-up of bids and offers on the Consolidated Book at the beginning of open outcry. However, as the trade is executed, the

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<sup>4</sup> A non-Customer is a market participant who does not meet the definition of Customer as defined in paragraph (c)(6) of Rule 15c3-1 under the Securities Exchange Act of 1934, as amended. See Rule 6.1(b)(29).

<sup>5</sup> The term "Consolidated Book" means the Exchange's electronic book of limit orders for the accounts of Public Customers and broker-dealers, and Quotes with Size. See Rule 6.1(b)(37).

Consolidated Book could update with newly-arriving electronically-entered bids and offers that have priority. Given the speed at which quotes can flicker in the Consolidated Book, Crowd Participants who have agreed to a transaction in open outcry do not know if they will actually participate on the trade until after execution.

In order to provide greater opportunity for bids and offers of Crowd Participants to participate in an open outcry transaction and therefore promote larger-sized negotiated transactions, the Exchange proposes to restructure its priority rules. As proposed, bids and offers of Crowd Participants would have priority over equal-priced bids and offers of non-Customers on the Consolidated Book that are ranked in time priority behind any equal-priced Customer bids and offers on the Consolidated Book. As proposed, equal-priced Customer interest would continue to be afforded priority over Crowd Participants in the execution of an open outcry transaction. In addition, consistent with the existing price/time priority presently applicable to bids and offers on the Consolidated Book, equal-priced non-Customer bids and offers ranked in time priority ahead of Customer interest will also be afforded priority over Crowd Participants in the execution of an open outcry transaction. The Exchange believes the proposed rule change strikes the appropriate balance between encouraging larger negotiated transactions in open outcry while at the same time protecting Customer interest on the Consolidated Book, and any interest that has time priority over such protected Customer interest.

To effect this proposed revision to its priority rules, the Exchange proposes to amend its rules as follows:

Rule 6.75. Priority and Order Allocation Procedures - Open Outcry. Rule 6.75(a) presently states that the highest bid shall have priority but where two or more bids for the same option contract represent the highest price and one such bid is displayed on the Consolidated

Book, such bid shall have priority over any bid at the post (i.e., the trading crowd). The Exchange proposes to amend Rule 6.75(a) by limiting the priority of bids in the Consolidated Book over bids in the trading crowd to just those bids for Customers along with non-Customers that are ranked in time priority ahead of such Customers.

The Exchange notes that the changes made to subsection (a) dealing with the priority of “bids” will also effect a corresponding change to the meaning of subsection (b) dealing with “offers”, although there will be no change to the rule text in subsection (b).

Rule 6.76. Order Ranking and Display – OX. Rule 6.76 governs order ranking, display and allocation of orders on the OX system. The Exchange is proposing new subparagraph (d) outlining the priority of bids and offers on the Consolidated Book against orders executed via open outcry in the Trading Crowd. The proposed text provides a step-by step-description of the order of priority afforded bids and offers of both Customers and non-Customers on the Consolidated Book. The priority described in proposed subparagraph (d) is consistent with the proposed changes to Rule 6.75.

The Exchange also proposes to include language in subparagraph (d) specifying certain OTP Holder obligations under Section 11(a) of the Act. Specifically, pursuant to Section 11(a)(1)(G) of the Exchange Act and Rule 11a1-1(T) thereunder (the “G Rule”), OTP Holders may effect transactions on the Trading Floor for its own account [sic], the account of an associated person, or an account with respect to which it or an associated person has investment discretion provided that such transaction yields priority in execution to orders for the account of persons who are not OTP Holders or associated with OTP Holders. The proposed rule text will confirm that notwithstanding the proposed change to the priority rules governing open outcry trading, an OTP Holder effecting a transaction on the Trading Floor for its own account, the

account of an associated person, or an account with respect to which it or an associated person has investment discretion pursuant to the “G Rule” must still yield priority to all equal-priced bids or offers on the Consolidated Book.<sup>6</sup> The proposed rule text is based on the rules of the Chicago Board Options Exchange, Inc. (“CBOE”) and NYSE MKT LLC (“NYSE MKT”) on behalf of NYSE Amex Options.<sup>7</sup>

The Exchange believes that including a description of open outcry priority procedures in Rule 6.76 will serve as a useful cross reference to the priority procedures of Rule 6.75. Including such a cross reference is consistent with similar rule structure by the CBOE and NYSE MKT.<sup>8</sup>

Rule 6.47. Crossing Orders – OX. Rule 6.47 outlines the procedures used when a Floor Broker attempts to cross two orders in open outcry. Under current rules, Floor Brokers must trade against all equal-priced Customer and non-Customer bids and offers on the Consolidated Book before effecting a cross transaction in the Trading Crowd. The Exchange proposes to make applicable changes to Rule 6.47 to conform the priority rules applicable to open outcry cross transactions to the proposed changes to Rule 6.75(b) [sic]. Accordingly, the Exchange proposes to amend the procedures for each crossing scenario described in Rule 6.47 by stating that Floor Brokers, when crossing two orders in open outcry, must yield priority to equal and better-priced Customer bids or offers on the Consolidated Book along with any non-Customer bids and offers ranked ahead of such Customers bids and offers.

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<sup>6</sup> The Exchange notes that at this time, none of the OTP Holders that currently operate on the Exchange’s Trading Floor as Floor Brokers enter orders for their own account, the account of an associated person, or an account with respect to which it or an associated person has investment discretion. The Exchange notes, however, that FINRA, on behalf of NYSE Regulation, monitors whether Floor Brokers comply with Section 11(a) of the Act.

<sup>7</sup> See CBOE Rule 6.45A(b)(i)(D) and NYSE MKT Rule 910NY.

<sup>8</sup> See CBOE Rule 6.45A(b) and NYSE MKT Rule 964NY(e).

Pursuant to these proposed rule changes, Floor Brokers would continue to be required to trade against equal and better-priced Customer bids and offers on the Consolidated Book along with bids and offers of non-Customers that are ranked ahead of such Customers before attempting a cross transaction. Consistent with the proposed change to Rule 6.75(a), Floor Brokers would not be required to trade against equal-priced non-Customer bids and offers that are ranked behind such Customer and non-Customer bids and offers. The Exchange believes that affording priority to Crowd Participants ahead of such non-Customer interest on the Consolidated Book will create an increased incentive for block-sized transactions on the Trading Floor.

### **Examples**

The revised priority and order allocation procedures would be applied as follows.

Ranking of bids on the Consolidated Book (assume this for all examples)

Customer #1	\$1.00 bid x 100
Non-Customer #1	\$1.00 bid x 50
Customer #2	\$1.00 bid x 100
Non-Customer #2	\$1.00 bid x 200
Non-Customer #3	\$1.00 bid x 100

#### Example 1

A Floor Broker enters the trading crowd with an order to sell 1000 contracts and after calling for a market, Crowd Participants respond with a collective bid of \$1.00 for 1000 contracts. Under current rules, the Floor Broker would be required to execute against all five bids on the Consolidated Book for a total of 550 contracts, thereby limiting the Crowd Participants to 450 contracts. Pursuant to the proposed revised order of priority, the Floor Broker would execute the order as follows:

Customer #1	100 contracts
Non-Customer #1	50 contracts
Customer #2	100 contracts
Trading Crowd	750 contracts

As such, the Floor Broker would execute 750 contracts with Crowd Participants instead of 450 contracts. Consistent with proposed changes to Rule 6.75(a), the Floor Broker yielded priority to all equal-priced Customer interest (Customers #1 and #2), along with bids of non-Customers ranked ahead of such equal priced Customers (non-Customer #1). After affording priority to such bids on the Consolidated Book, the Floor Broker executed the balance of the order against bids from participants in the trading crowd. Because there was sufficient size to execute the entire balance of the order in the Trading Crowd, there is no further allocation to the non-Customers ranked behind Customer interest on the Consolidated Book.

#### Example 2

A Floor Broker enters the trading crowd with an order to sell 1300 contracts and a contra order to buy 500 contracts. After calling for a market, Crowd Participants respond with a bid of \$1.00 for 500 contracts. The Floor Broker then announces his intent to execute a Non-Facilitation Cross at \$1.00 pursuant to Rule 6.47(a). Under current rules, the Floor Broker would be required to execute against all five bids on the Consolidated Book for a total of 550 contracts, thereby limiting the Crowd Participants and the Floor Broker cross order to an aggregate of 750 contracts. Pursuant to the proposed revised order of priority, the Floor Broker would execute his sell order as follows:

Customer #1	100 contracts
Non-Customer #1	50 contracts
Customer #2	100 contracts
Trading Crowd	500 contracts
Broker Cross	500 contracts
Non-customer #2	50 contracts

Consistent with proposed changes to Rule 6.75(a), the Floor Broker yielded priority to all equal-priced Customer interest (Customers #1 and #2), along with bids of non-Customers ranked ahead of those equal-priced Customers (non-Customer #1). After affording priority to such bids on the Consolidated Book, the Floor Broker traded with members of the trading crowd and then crossed his sell order against his contra-side buy order. The Floor Broker then traded the balance of his sell order against the non-Customer bids that were ranked behind Customer interest on the Consolidated Book. The non-Customer bids were executed pursuant to their ranking on the Consolidated Book based on time priority.

Example 3

A Floor Broker enters the trading crowd with an Agency Order to sell 1000 contracts and a buy order for the proprietary account of an OTP Firm to facilitate the entire size of the Agency Order ("Facilitation Order"). After calling for a market, Crowd Participants respond with a bid of \$1.00 for 1000 contracts. The Floor Broker then announces his intent to execute a Facilitation Cross at \$1.00 pursuant to Rule 6.47(b). Under current rules, the Floor Broker would be required to first execute against all five bids on the Consolidated Book for a total of 550 contracts, leaving 450 contracts to be allocated between the Facilitation Order and the trading crowd. Of the 450 remaining contracts, the Facilitation Order would be allocated 180 contracts (40% of 450) with 270 going to the trading crowd. Pursuant to the proposed revised order of priority, the Floor Broker would execute his sell order as follows:

Customer #1	100 contracts
Non-Customer #1	50 contracts
Customer #2	100 contracts
Firm Facilitation	300 contracts
Trading Crowd	450 contracts



Consistent with proposed changes to Rule 6.75(a), the Floor Broker yielded priority to all equal-priced Customer bids (Customers #1 and #2), along with bids of non-Customers ranked ahead of those equal-priced Customers (non-Customer #1). After affording priority to such bids on the Consolidated Book, the Floor Broker was left with 750 contracts. The Facilitation order is entitled to participate on 40% of the balance of the Agency Order (300 contracts) and the balance of 450 contracts would be allocated to members of the trading crowd.

The Exchange believes that providing greater opportunity for large-sized orders to execute in open outcry while also protecting Customer interest will encourage participants to send more liquidity to Floor Brokers, thereby resulting in a larger pool of liquidity on the Exchange that would not otherwise be available electronically. The Exchange further believes that the proposed change in priority will provide an incentive for Crowd Participants, including Floor-based Market Makers, to provide deeper liquidity when participating in open outcry transactions as there will be greater certainty of an execution. The Exchange notes that affording priority to Crowd Participants over non-Customers is not a new or novel idea. Other hybrid markets such as the CBOE and NYSE Amex Options afford Crowd Participants priority over non-Customer electronic bids and offers on their respective market.<sup>9</sup> The only substantive difference between the priority procedures being proposed in this filing and those presently in place at the CBOE and NYSE Amex Options is that the Exchange proposes to afford priority to bids and offers of non-Customers on the Consolidated Book, ranked ahead of any equal-priced Customers on the Consolidated Book, over members of the trading crowd. On the CBOE and NYSE Amex Options, crowd participants have priority over all equal priced non-Customers in the Consolidated Book.

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<sup>9</sup> Supra Note No. 7.

### Non-Substantive Rule Changes

The Exchange is also proposing to make non-substantive changes to existing rule text contained in Rules 6.47 and 6.75. Currently, the terms “Book” and “Consolidated Book” are both used in Rule 6.47 when referring to the Exchange's electronic book of limit orders for the accounts of Public Customers and broker-dealers, and Quotes with Size. The Exchange now proposes to standardize the rule language by replacing “Book” with the defined term “Consolidated Book”.<sup>10</sup> In addition, Rules 6.47 and 6.75 currently use the terms “in” and “on” when referring to orders, quotes or bids and offers contained on/in the Consolidated Book. The Exchange now proposes to standardize the rule language by replacing “in” with “on” whenever referring to orders, quotes and bids and offers on the Consolidated Book.

### Implementation

The Exchange will announce the implementation date of the proposed rule change by Trader Update to be published no later than 90 days following approval. The implementation date will be no later than 90 days following the issuance of the Trader Update.

## 2. Statutory Basis

The proposed rule change is consistent with Section 6(b)<sup>11</sup> of the Securities Exchange Act of 1934 (the “Act”), in general, and furthers the objectives of Section 6(b)(5),<sup>12</sup> in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in facilitating transactions in securities, and to remove impediments to and perfect the mechanisms of a free and open market and a national market system. The Exchange believes that the

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<sup>10</sup> See NYSE Arca Rule 6.1(b)(37).

<sup>11</sup> 15 U.S.C. 78f(b).

<sup>12</sup> 15 U.S.C. 78f(b)(5).

proposed rule change will remove impediments to and perfect the mechanism of a free and open market by restructuring relative priorities between bids and offers made on the floor compared to non-Customers in the Consolidated Book in order to provide an incentive both for Floor Brokers to represent orders in open outcry and for Floor-based Market Makers to participate in open outcry transactions. The Exchange believes that the negotiated nature of open outcry transactions lends itself to larger-sized transactions than the liquidity that is generally available electronically and the proposed rule change would encourage greater participation in such open outcry trading by reducing the potential that a negotiated transaction would be broken up. The Exchange therefore believes that affording priority to Crowd Participants ahead of certain non-Customer interest on the Consolidated Book creates an opportunity for increased participation on open outcry transactions, which should result in larger-sized negotiated transactions, while at the same time protecting Customer interest. The Exchange believes that this in turn will lead to greater competition for orders creating a more robust open outcry market, which should benefit investors who choose to send orders to the Exchange. The Exchange further believes that protecting non-Customer interest on the Consolidated Book that is ranked ahead of Customer interest is consistent with just and equitable principles of trade because it maintains the Exchange's existing price/time priority rules by protecting interest that has time priority over Customer interest that has priority.

In addition, the proposed rule change is consistent with Section 11A(a)(1)(C) of the Act,<sup>13</sup> in which Congress found that it is in the public interest and appropriate for the protection of investors and the maintenance of fair and orderly markets to assure, among other things, the economically efficient execution of securities transactions. The Exchange notes that the

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<sup>13</sup> 15 U.S.C. 78k-1(a)(1)(C).

proposed rule change is also consistent with Section 11(a) of the Act and the rules thereunder. The Exchange believes that affording priority to OTP Holders present in the trading crowd over certain electronic non-Customer orders raises no novel issues under Section 11(a) and the rules thereunder from a compliance, surveillance or enforcement perspective. In other words, OTP Holders on the Floor are currently required to comply and are subject to review for compliance with Section 11(a), and the rules thereunder, when executing transactions in open outcry and notwithstanding the proposed rule change, they will still be required to comply with Section 11(a) and the rules thereunder. For example, in cases where an OTP Holder acting as a Floor Broker is trading for his own account and attempts to execute a transaction at the same price as one or more orders on the Consolidated Book, the Floor Broker, if he can rely on no exception other than the "G" exception (Section 11(a)(1)(G); Rule 11a1-1(T)), must, in addition to complying with the other requirements of the "G" exemption, yield to all orders in the Consolidated Book at the same price if the Floor Broker has no ability to determine that an order in the Consolidated Book is not the order of a non-OTP Holder.<sup>14</sup>

The restrictions set forth in NYSE Arca Rule 6.76(d)(4) would not limit in any way the obligation of OTP Holders, while acting as a Floor Broker or otherwise, to comply with Section 11(a) or the rules thereunder. For example, Floor Brokers cannot avoid or circumvent their obligations under Section 11(a) when executing a transaction on the floor simply by transferring

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<sup>14</sup> The Exchange notes that only orders that are represented by a Floor Broker are eligible for crossing via the Solicited Order procedures. If the Floor Broker represents an order for its own account, the account of an associated person, or an account with respect to which it or an associated person has investment discretion, the member order must satisfy the requirements of Section 11(a) of the Act and the rules thereunder. The Exchange has previously represented that OTP Holders (members) may not rely on the exception found in Section 11(a)(1)(G) of the Act when utilizing the Solicited Order procedures. See Securities Exchange Act Release No. 54238 (July 28, 2006) 71 FR 44758, 44763 at n.43 (August 7, 2006).

that order to another OTP Holder on the floor or to an OTP Holder off the floor of the Exchange. OTP Holders must ensure compliance with Section 11(a) and the rules thereunder, including by relying upon an exemption such as those listed above.

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The Exchange believes that competition for participation in open outcry transactions will be enhanced by allowing the Crowd Participants to compete at price points that were previously unavailable because of non-Customer orders on the Consolidated Book, thereby promoting competition by encouraging participation in large-sized negotiated transactions. In addition, because this proposal seeks to adopt rules that are more closely aligned with those of other Exchanges [sic] operating a hybrid market, the Exchange does not believe that the proposed rule changes will create an undue burden on other markets. Rather, the Exchange believes that not approving this proposed rule change would place the Exchange at a competitive disadvantage vis-à-vis other Exchanges that operate a trading floor.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

No written comments were solicited or received with respect to the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- (A) by order approve or disapprove the proposed rule change, or

- (B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. The Commission solicits comment on the impact of NYSE Arca's proposal to revise its priority scheme with respect to non-Customer orders on the Exchange's Consolidated Book during the execution of an order in open outcry on the Exchange's floor. Commenters are invited to address the impact, if any, of the proposed rule change on competition on the Exchange's floor and on its Consolidated Book, including the impact, if any, on market participants' incentives to post interest on the Consolidated Book, and the reasons for any such view. In the Notice, the Exchange argues that the proposal would create an opportunity for increased crowd participation in open outcry transactions and would lead to greater competition for orders brought to the Exchange's floor. Commenters are invited to address these arguments. Further, in the Notice, the Exchange states that the proposal will more closely align the Exchange's rules with those of other exchanges operating a hybrid market. Commenters also are invited to provide their views on the differences and/or similarities between NYSE Arca's proposal and the pertinent CBOE and NYSE MKT priority rules and how, if at all, the overall priority structure of the three exchanges (public customer/pro rata in comparison to price/time) impacts their view. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or

- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-NYSEArca-2014-04 on the subject line.

Paper comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-NYSEArca-2014-04. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549-1090, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer

to File Number SR-NYSEArca-2014-04, and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>15</sup>

Kevin M. O'Neill  
Deputy Secretary

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<sup>15</sup> 17 CFR 200.30-3(a)(12).